WTO SERVICES TRADE NEGOTIATIONS

This paper uses a question-and-answer format to provide background information on the WTO General Agreement on Trade in Services (GATS), and the GATS negotiations that began in January 2000. Issues addressed include the nature of trade in services; their importance to the U.S. economy; GATS structure, terminology, and obligations; and information on four issues carried over from the Uruguay Round (movement of natural persons, safeguards, air transport, and maritime transport). The final section of the paper provides sources of additional information, most available via the internet.

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What are services?

Services are what most Americans do for a living. Service industries account for nearly 80 percent of U.S. employment and GDP. U.S. exports of commercial services (i.e., excluding military and government) were $246 billion in 1998, supporting over 4 million services and manufacturing jobs in the United States.

Cross-border trade in services accounts for more than 22 percent of world trade, or about $ 1.3 trillion annually. U.S. services exports have more than doubled over the last ten years, increasing from $117 billion in 1989 to $246 billion last year.

U.S. services compete successfully worldwide. Major markets for U.S. services include the European Union ($83 billion in private sector 1998 exports), Japan ($31 billion), and Canada ($20 billion). At $12 billion, Mexico is presently the largest emerging market for exports.

Services are critically important to an efficient economy. Service sectors include:

- Essential infrastructure systems like telecommunications, finance, energy services, transportation, and distribution;

- Professional services like accounting, law, architecture, and engineering; and

- Private segments of healthcare and education and training services.

- Services also include the important activities related to travel and tourism, as well as royalty and licensing transactions. All travel-related purchases by visitors to the United States (e.g., transportation, lodging, and dining expenses) are counted as exports, as are sales of royalties and licensing fees (such as for manufacturing processes). Taken together, these account for 52 percent of U.S. cross-border services exports.

How are services traded and what are "modes of supply"?

From an economic perspective, services are traded on a cross-border basis as well as through sales of foreign-based affiliates. Both forms of trade are significant to the balance of payments and U.S. competitiveness.

The GATS further separates services trade into four modes of supply: cross-border supply, consumption abroad, commercial presence, and the presence of natural persons. Commercial presence is simply another way of describing a majority-owned or otherwise controlled foreign affiliate, while the other three modes represent different means of providing services across borders (see below). These categories are used to more precisely capture the manner in which services are provided and thereby facilitate the process of identifying and subsequently disciplining restrictions to services trade.

Cross-border Trade

Cross-border trade in services is a relatively straightforward exchange whereby:

- The service is provided in one country to a customer in a second country without either party traveling, e.g., a U.S. investment banker arranges financing for a construction project being undertaken by a client in London -- this corresponds to the GATS mode of cross-border supply.

- The customer travels from abroad to the service provider's country to receive a service, e.g., an individual from Venezuela travels to Miami to receive medical treatment – this corresponds to the GATS mode of consumption abroad and results in a U.S. export of healthcare services.

- An individual travels to the customer's country on a temporary basis to provide a service, e.g., a U.S. engineering consultant travels to Brazil to provide advice on the construction of a waste water treatment plant -- this corresponds to the GATS mode of temporary presence of natural persons.

U.S. cross-border services exports measured $246 billion in 1998 (most recent year), and are broken down as follows:

Industry	Percentage of U.S. services exports, 1998
Travel and tourism	29
Royalties and license fees	15
Freight transportation	10
Business, professional, and technical	10
Passenger fares	8
Finance and insurance	7

Education	4
Telecommunications	2
Other	15

Cross-border exports of services contribute directly to the balance of payments. In 1998, the U.S. services surplus of $80 billion offset 33 percent of the U.S. merchandise trade deficit.

The largest export markets for U.S. cross-border services trade are the European Union (34 percent), Japan (13 percent), Canada (8 percent), and Mexico (5 percent).

Affiliate Trade

Sales of services by foreign affiliates of U.S. firms take place when a U.S. firm establishes a presence in a foreign country for the purpose of providing services, e.g., Bell Atlantic builds and operates a wireless telecommunications company in Southeast Asia -- this corresponds with the GATS mode of commercial presence (Mode 3).

Affiliate sales by U.S. companies measured $258 billion in 1997, broken down as follows (note: affiliate data at the industry level of detail lag behind aggregate data by one year):

Industry.	Percentage of U.S. affiliate sales, 1997
Insurance	18
Computer and data processing	13
Public utilities (electric power, water, and sewer)	8
Wholesale trade	6
Transportation	4
Motion pictures	3
Accounting	3
Other, including finance, telecom, and electric power	45

Investment income earned by foreign affiliates is recorded in the balance of payments. (In 1998, the United States earned $103 billion in direct investment income (from both goods and services affiliates), offsetting 42 percent of the U.S. merchandise trade deficit in the balance of payments).

Foreign affiliates of U.S. firms are a powerful source of U.S. competitiveness for both service and manufacturing firms. Many U.S. manufacturing companies, such as IBM and General Electric, maintain services affiliates abroad to finance and distribute their products, as well as to provide after-sales services such as systems integration or equipment maintenance. Often, service contracts well exceed the value of the merchandise provided.

Foreign affiliates also enable U.S. firms to maintain greater control over their intellectual property (e.g., patents, trademarks, proprietary processes or technology) than licensing or other partnership arrangements. This in turn enables U.S. firms to sustain their competitive advantage.

For many U.S. service firms, establishing foreign affiliates is the only way to expand into new markets. For example, wireless telephone service providers or electric power generators must establish a commercial presence to be physically close to their customers.

For other U.S. service firms, foreign affiliates are essential to serving their global clients. Advertising agencies, accounting firms, and telecommunications providers gain a competitive advantage by being able to provide a consistent level of service wherever their clients are operating. This in turn enables U.S. manufacturing firms to better leverage their resources, for example, by permitting the manufacturer to integrate telecommunication networks, accounting systems, or advertising programs globally.

The largest markets for U.S. sales of services by affiliates are Europe (57 percent), Canada (9 percent), and Japan (9 percent).

What is the GATS?

The General Agreement on Trade in Services (GATS) is the first multilateral, legally enforceable agreement covering trade and investment in services. The GATS is designed to reduce or eliminate governmental measures that prevent services from being freely provided across national borders or that discriminate against locally-established service firms with foreign ownership.

The GATS:

- Provides a legal framework for addressing barriers to trade and investment in services,
- Includes specific commitments by WTO member countries to restrict their use of those barriers, and
- Provides a forum for further negotiations to open services markets around the world.

What are the major obligations contained in the GATS?

The GATS framework lays out the general obligations for trade in services in much the same way that the General Agreement on Tariffs and Trade (GATT) does for trade in goods. Most-favored-nation treatment, market access and national treatment are three of the important principles included in the general framework of the GATS.

Most-favored-nation treatment: All countries guarantee most-favored-nation (MFN) treatment in all service sectors, unless they have listed an exemption for a specific sector. An MFN guarantee means a country will treat the service supplier of another member no less favorably than it does the service suppliers of any other member.

MFN Exemptions List: An MFN exemption is taken when a country explicitly states it will not guarantee most-favored-nation treatment in a particular services sector to service suppliers from other WTO member countries. Usually these exemptions are taken when some countries have been granted special or preferential access to a sector.

MFN exemptions can only be taken when a country joins the WTO (except in the case of sectoral negotiations extended after the end of the Uruguay Round). In principle they should not exceed 10 years and are subject to review after five (this review began in November 1999 and is continuing into 2000). MFN exemptions are listed separately from a country's schedule of commitments. The list of MFN exemptions is relatively easy to read. A country includes the following in its MFN exemption list: the sector, the measure inconsistent with MFN, the country/countries to which the exemption applies, the duration of the exemption, and the reason for the exemption.

Market Access and National Treatment: When a country lists a sector in its schedule and makes a specific commitment in its schedule, that country agrees to allow foreign service suppliers to enter its market to provide a service (market access) and agrees to treat foreign suppliers under the same terms and conditions as it treats its domestic suppliers (national treatment). A country can list limitations on market access and national treatment in this “schedule of commitments.”

By making a commitment of MFN, national treatment or market access in a particular service sector, a country agrees to adhere to the principles as defined by the agreement, subject to the limitations listed in its schedule. Just as tariff schedules are commitments not to raise tariffs in the future above the level scheduled, a GATS scheduled commitment means a country has agreed not to become more restrictive in that particular service sector.

Any violations of a country's commitments, including guarantees for MFN, market access and national treatment, can be addressed through the WTO dispute settlement mechanism. Under the dispute settlement mechanism, a country may be required to give compensation in trade benefits if a panel finds that it has not adhered to its commitments and the country does not make the necessary changes to its trade regime.

What is meant by positive listing or bottom-up scheduling methodology?

The GATS employs a unique approach in that some obligations (such as MFN) are applied to all service sectors unless specifically exempted, while others (national treatment and market access, and several general obligations tied to them) are not applied to any service sectors unless specifically included in members’ schedules -- a positive-listing or bottom-up method.

To include specific industry sectors, each country makes commitments to accord national treatment and market access in the separate schedules of commitments. This process is called “positive listing” or “bottom-up” because each country must affirmatively list each sector. By contrast, negative listing or a top-down approach would mean that the obligations apply to all sectors unless a country specifically lists an exception.

Why are the schedules of commitments, supplemental schedules, and lists of MFN exemptions important?

All members of the WTO are signatories to the GATS framework agreement and must have a schedule of GATS commitments. Yet, while all signatories committed themselves to the GATS principles of national treatment, market access, and MFN, each country made different commitments for different service sectors during the Uruguay Round.

At the end of the Uruguay Round, the GATS called for extended negotiations in four service sectors: basic telecommunications, financial services, movement of natural persons, and maritime transport services. Negotiations in the first two sectors concluded in 1997. Negotiations on movement of natural persons concluded in 1995. Negotiations on maritime transport services were suspended in 1996 and must be resumed in the context of the next GATS round.

A country's complete set of GATS commitments thus could consist of several documents, beyond its original Uruguay Round commitments and list of MFN exemptions, as some countries may have supplemental schedules for one or more of the extended sectoral negotiations.

All of these documents must be consulted in order to determine the commercial significance of a country's commitments under the GATS. At the request of WTO Members, the WTO Secretariat is developing an electronic "looseleaf" version of country schedules and MFN exemptions. While this version would not have any legal status, it should help those outside the WTO better understand country commitments.

Why do we need another round of GATS negotiations?

While the GATS broke new ground by establishing a framework of rules applicable to trade in services, it did not bring about significant services trade liberalization. Instead, the GATS effectively established a baseline from which future negotiations would proceed. The objective of GATS 2000 then is to broaden and deepen the coverage of the agreement by strengthening some of the general principles, expanding the scope of sectors included, and eliciting more liberal commitments to accord national treatment and market access to U.S. service providers.

Why is regulation important to services? What are the major barriers to services trade?

A major barrier to services trade is discriminatory or non-transparent regulatory policy. Service industries are heavily regulated. From telecommunications to finance to medicine, government regulation plays an integral role in defining the industry and determining how many firms can participate and under what terms and conditions. The ongoing waves of "deregulation" are indicative of a regulatory shift in favor of market mechanisms, but the fundamental regulatory functions endure.

Foreign service firms can be adversely affected by explicit discriminatory policies (e.g., foreign equity caps) or market access limitations (e.g., economic needs tests), as well as less clearly defined limitations that result from a non-transparent policy process (e.g., regulations change without notice, publication, or any input into the process).

What are LDC concerns regarding the movement of persons?

Some LDCs continue to request that developed countries make commitments that would provide greater access to individuals (versus companies) as service suppliers. Interestingly, and in contrast to the Uruguay Round, some LDCs have identified their services export interests more broadly, in terms of specific sectors rather than only in terms of movement of persons issues. Sectors identified include audiovisual services, tourism, private healthcare, computer services, and professional services

Should there be additional safeguard provisions in the GATS?

As part of work left over from the Uruguay Round, some developing countries advocate inclusion of safeguard provisions in the GATS, to be invoked if a country is facing a surge of services activity that threatens domestic service providers. The United States is not convinced of the need for or feasibility of such provisions but is willing to consider them in the context of further services liberalization.

What is the status of air transportation services under the GATS?

The only sector excluded from the GATS is most air transport services – that is, traffic rights and related services typically covered under bilateral civil aviation agreements. Traffic rights were excluded by consensus during the Uruguay Round, since most WTO Members were unprepared to abandon the existing framework of bilateral agreements. The GATS requires a review of this exclusion, which is continuing in 2000.

What is the status of maritime services negotiations?

Maritime transport services were subject to follow-on negotiations after the Uruguay Round. Those negotiations were suspended in June 1996 when it became clear that virtually no WTO Member was willing to meet the ministerial mandate for the negotiations – that is, to take on GATS commitments "leading to the elimination of restrictions within a fixed period of time." Countries instead wanted to use the negotiations to bind in the GATS their existing, restrictive regimes. Cabotage trade, the movement by water of cargo between two points in the same country (for the U.S., the Jones Act) was not part of the negotiation.

The GATS Council decision that suspended the negotiations in June 1996 also required resumption of the negotiations in the context of the next GATS round.

Additional Information Resources:

Testimony and Speeches

- Services in the New Round, testimony by Ambassador Charlene Barshefsky before the Senate Banking Committee, Washington, DC, November 2, 1999, www.ustr.gov/testimony/barshefsky_32.html

- Approaching the New Round: American Goals in Services Trade, testimony by Ambassador Susan Esserman before the Senate Finance Subcommittee on Trade, Washington, DC, October 21, 1999, www.ustr.gov/testimony/esserman_12.html

- Services in the World Trading System, speech by Ambassador Richard Fisher to the World Services Congress Atlanta, Georgia, November 1, 1999, www.ustr.gov/speeches/fisher/fisher_17.html

World Trade Organization Publications:

- Country Schedules of Specific Commitments www.wto.org/wto/services/22-specm.htm

- Guide to Reading the GATS Schedules of Specific Commitments and the Lists of Article II (MFN) Exemptions: www.wto.org/wto/new/guide1.htm

- Services - Rules for Growth and Investment: www.wto.org/about/agmnts5.htm

- Text of the General Agreement on Trade in Services: www.wto.org/wto/services/gatsintr.htm

- Protocols to the GATS (on Financial Services, Movement of Natural Persons, and Basic Telecommunications): www.wto.org/wto/services/prots.htm

- Sectoral papers prepared as part of the GATS Council Information Exchange: www.wto.org/wto/services/w65.htm

U.S. International Trade Commission publications:

- Recent Trends in U.S. Services Trade (1999 Annual Report): ftp://ftp.usitc.gov/pub/reports/studies/PUB3198.PDF

- Examinations of GATS Schedules of Commitments: Major Trading Partners: European Union, Canada, Mexico, and Japan; South America; Asia/Pacific; Eastern Europe: ftp://ftp.usitc.gov/pub/reports/studies/PUB3127.PDF (hard copies of all USITC studies are available through Richard Brown, tel. 202-205-3438, fax 202-205-2359.

U.S. Department of Commerce Data and General Information/Publications about the U.S. Services Sector:

- USDOC, Bureau of Economic Analysis: www.bea.doc.gov

- USDOC, International Trade Administration, Service Industries and Finance, www.ita.doc.gov/sif

OECD Publication:

- Assessing Barriers to Trade in Services: Cross-cutting ("Formula") Approaches to Multilateral Services Negotiations, TD/TC/WP(99)42/FINAL, www.oecd.org/ech/seattle/services.htm